INTERCO

1990 ANNUAL REPORT

INTERCO Today is a major manufacturer of furniture and a manufacturer and retailer of footwear, through two operating groups.

Furniture and Home Furnishings Group is a major manufacturer and distributor of quality furniture and home furnishings principally in the United States. There are 39 factories and seven major distribution centers and consolidation warehouses located primarily in the Southeastern part of this country.

Footwear Manufacturing and Retailing Group styles, manufactures and distributes primarily men's footwear, and a broad range of athletic footwear, principally in the United States, Australia, Canada, Europe and Mexico. There are nine factories and eight major distribution centers in operation. The group also operates 558 retail shoe stores and leased shoe departments in 40 states, as well as in Australia, Canada and Mexico.

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To Our Shareholders:

Fiscal 1990 was a year of dramatic change as INTERCO implemented its corporate restructuring:

- progress was made toward completion of the asset-sale program, although proceeds in the aggregate fell short of original projections;
- on the operations side, we focused on our four core companies—Broyhill Furniture Industries, Inc., The Lane Company, Incorporated, The Florsheim Shoe Company and Converse Inc.—putting in place a number of programs aimed at improving gross profit margins; and
- a wide-ranging cost reduction and operating efficiencies program was implemented at the four core companies and corporate headquarters.

Asset Sale Program

Proceeds from the sales of Ethan Allen Inc. and Central Hardware Company were less than originally expected. Contributing were the collapse of the high-yield bond market, a frequently used financing source, a tightening in the credit markets and higher interest rates. Besides negatively affecting selling prices, these factors also contributed to the program's taking longer to complete than anticipated.

Proceeds from other asset sales during the year generally met our projections.

Asset-sale proceeds, including those from the late fiscal 1989 sales of Londontown Corporation and The Biltwell Company, Inc., were applied to repay more than $900 million of the $1.15 billion asset-sale bridge loan. Still on the market are a few operating companies, which will bring less than the $244.5 million balance of the bridge loan. To reduce this shortfall, we identified other assets to be sold, including Florsheim's headquarters building in Chicago and the Hy-Test safety shoe subsidiary.

Core Company Operations

The core companies embarked on their own restructuring programs, eliminating less profitable product lines and operations. Importantly, each company has promising new products and marketing programs which are discussed later in this letter.

Operating results of the core companies in fiscal 1990 did not reach our original expectations. Core company sales totaled $1.47 billion, compared with $1.57 billion in fiscal 1989. Nonetheless, operating profits were up over the year-earlier figures—$137.7 million versus $127.4 million. Operating earnings of the core footwear companies rose 21.8 percent, while results of the furniture companies were about even. We think it is significant that three of the core companies, Broyhill, Lane and Florsheim, increased their market shares in fiscal 1990. Converse positioned itself for a resumption of a more favorable sales and earnings trend by liquidating excess inventory and introducing the new *Magic* and *Evolo* product lines.

Cost Reduction Efforts

During the year, we identified cost reductions and operating efficiencies that will total more than $75 million annually. Because of implementation costs and timing, however, about half that amount was realized in fiscal 1990. Going forward, the company will continue to benefit from cost savings.

Further Restructuring Needed

As indicated, fiscal 1990 had its pluses and minuses. As the year progressed, it became increasingly obvious that our balance sheet requires restructuring to ensure the company's long-term viability. Further, with asset-sale proceeds and operating earnings below projections published in December 1988, it became apparent INTERCO would not meet the May 7, 1990, deadline for repayment of the bridge loan facility, and that future principal and interest payments were in jeopardy.

Simply put, the challenges confronting our company revolve around one basic fact: the company has too much debt. Therefore, we hired J.P. Morgan & Co. to evaluate various alternatives in order to enhance the financial position of the company. After an in-depth study, it was decided the best course of action would be to adjust the company's capitalization.

This spring, we reached agreement with the steering committee of our bank lending group on basic terms for restructuring our bank debt and the full bank group extended to October 1, 1990, certain loan payments due May 7, 1990, including the final payment on the asset-sale bridge loan, allowing time for completion of the negotiation and documentation of the amendment of the bank credit agreement. The terms of the proposed amendment, which are presently being considered by the bank group, include incorporation of all of INTERCO's existing bank debt into a new six-year term loan and a continuing credit facility for the company's working capital needs, along with an expanded letter of credit facility.

To provide further relief from our highly-leveraged position, we have also announced a restructuring plan for our subordinated debt and preferred stock. If the plan is accepted, holders of the 13¾ percent senior subordinated debentures due 2000 would be entitled to exchange those debentures for newly issued shares of INTERCO common stock and a new issue of accrual convertible debentures due 2000; holders of the subordinated discount debentures due 2003 and the 14½ percent junior pay-in-kind subordinated debentures due 2003 would be entitled to exchange them for newly issued shares of INTERCO common stock.

We will also solicit shareholder approval to reclassify the outstanding shares of Series D $7.75 cumulative convertible preferred stock and Series E preferred stock into shares of common stock, and to implement a reverse-split of the common stock to accommodate the shares to be issued in the restructuring.

The successful conclusion of this restructuring will significantly improve the company's balance sheet and reduce our annual cash-interest requirements. The restructuring will also offer shareholders an opportunity to participate in the growth of our basic businesses: having received relief from an onerous debt burden, INTERCO's after-tax profits should benefit from the inherent strengths of the core companies.

Core Company Strengths

The completion of the proposed recapitalization will leave INTERCO with four core companies, Broyhill, Lane, Florsheim and Converse, which share common characteristics that augur well for a resumption of a positive sales and earnings trend:

- all have developed well established consumer franchises, with high brand recognitions;
- all have good market shares in highly fragmented industries;
- all have very efficient manufacturing operations; and
- all have ample capacity to handle additional business without large capital expenditures.

Broyhill

Broyhill, founded in 1926, has long been recognized as a pioneer in the introduction of mass production techniques to the furniture industry.

The company is well situated within the furniture industry, producing complete lines of medium and upper-medium priced bedroom, dining room, living room and occasional furniture. Its market share of 3 percent makes it one of the industry's largest companies.

Programs are in place which hold promise for further market share gains. A recently introduced line of casual, rustic pine furniture under the *Timbertown* brand name has been well received by consumers.

Broyhill's strategic plan targets five key market segments: 1) increased market penetration of department stores and national and regional furniture chains; 2) expanded Showcase Gallery Program, which includes more than 300 retail locations; 3) further penetration of the independent furniture dealer market with its pioneering advertising and merchandising assistance program; 4) increased Contract Division sales to hospitality and health care industries; and 5) attractive potential in the rental furniture market and catalog sales.

Lane

The *Lane* name is synonymous with cedar chests, a product category that it dominates and which formed the foundation for a substantial expansion into other furniture categories. While begun in 1912 as a cedar-chest maker, Lane today offers more than 5,000 items. Its product mix is approximately 40 percent reclining products, 35 percent wood furniture and 25 percent upholstery and other.

The Lane Company competes in the upper-medium and higher price ranges, which means that styling and quality are more important than prices. In addition, Lane's price points make its product lines less sensitive to fluctuations in the economy.

Lane is marketing several new products that have excellent growth potential, including a line of reclining sofas by its Action Industries subsidiary.

Other market thrusts are planned in fiscal 1991, including geographic expansion of product lines whose sales currently are concentrated in the eastern part of the United States. Plans are under way to combine more product offerings under the *Lane* label to capitalize on the high level of consumer recognition. Lane is also expanding its Gallery program, in which dealers commit floor space to its products.

Florsheim

Florsheim, a well known brand name that traces its roots to 1892, is clearly the nation's largest manufacturer and retailer of men's quality dress and dress casual footwear. In its middle to upper price ranges, Florsheim commands about a 20 percent market share.

While nearly 100 years old, Florsheim has adapted to the times, having restructured its manufacturing operations, reducing the number of domestic plants and increasing manufacturing efficiencies.

In addition, Florsheim recently completed a reevaluation of its retail locations, repositioning, closing or downsizing its company-operated stores, as appropriate. In a significant product mix shift, the company decided to sell only Florsheim shoes in its stores, capitalizing more fully on the brand's reputation, while at the same time enhancing profit margins.

Complementing this strategic approach was the introduction of a line of Florsheim dress and casual shoes in the $60 to $80 mid-price retail range. These highly competitive products have met with excellent consumer acceptance.

Florsheim remains optimistic about the potential of its Express Shop program to add incremental sales and to improve operating margins: a menu-driven computer console offers customers any style, color and size of shoe from Florsheim's complete product line.

With exports accounting for only 10 percent of Florsheim's volume, international markets, particularly Europe and the Far East, provide an opportunity for increased sales.

Converse

Converse, founded in 1908, is the largest U.S. manufacturer and a major supplier of athletic footwear, with approximately 75 percent of its sales to men. While soft demand for canvas shoes adversely affected results the past couple of years, two new aggressively-marketed product lines are projected to make significant contributions to sales and earnings.

The company is optimistic about the prospects of a new line of men's athletic shoes under the *Magic* label. With Los Angeles Laker superstar Magic Johnson promoting the footwear, retailers have responded enthusiastically to the product introduction. The *Magic* line takes Converse into the "streetwear" market for the first time and offers at extremely attractive retail price points—the $60 to $80 range—a more reasonable alternative to competitors' shoes of similar quality normally selling for $100 or more.

In an effort to capitalize on the very strong women's athletic footwear market, where Con-

verse has traditionally had little presence, a new line of shoes under the *Evolo* label is being marketed. The spokesperson for the performance, sports training, tennis and walking shoes is tennis great Chris Evert.

Long identified with its men's basketball shoe line, Converse is a leading supplier to players and teams in the National Basketball Association, the National Collegiate Athletic Association, as well as many high schools. The company is well positioned to capitalize on the rising international popularity of basketball, particularly in Europe.

Children's shoes, which account for about 10 percent of revenues, are also receiving increased emphasis.

Balanced manufacturing and sourcing position Converse with unique flexibility in the industry; its North American production facilities and importing capabilities typically provide a 50-50 percent product mix.

Management, Board Changes

In November 1989, Harvey Saligman relinquished his position as INTERCO's Chief Executive Officer and on May 31, 1990, he will retire as Chairman of the Board. We are pleased that he will continue to serve on the Board of Directors.

In December 1989, Zane E. Barnes and Marilyn S. Lewis, and in May 1990 Charles J. Rothschild, Jr., retired from the Board of Directors after 11 years, 5 years and 12 years, respectively, of service. We appreciate the counsel and support they provided through the years.

Conclusion

While we are encouraged by recent events, much remains to be done. Clearly, we must restructure our balance sheet to make our debt burden more manageable. We would then be able to focus our full attention on the four core companies, which have in place sound strategies to increase their operating profits.

I want to close by thanking our employees for their outstanding efforts in these challenging times. Words of appreciation also go to our Board of Directors for their counsel, and to our suppliers and customers for their ongoing support.

All of us are working toward the same goal: guiding INTERCO through this period of dramatic change in order to ensure the company's long-term viability and growth.

Sincerely,

R B Loynd

Richard B. Loynd
President and Chief Executive Officer

Management's Discussion and Analysis of Results of Operations and Financial Condition

RESULTS OF OPERATIONS

As a result of the major recapitalization program undertaken by the company in the third quarter of fiscal 1989, the results of operations and the financial condition of the company as reflected in the financial statements for the current reporting period are generally not comparable to amounts reflected for prior year periods.

Prior to the restructuring, the operating results of the company were reported under four segments, namely, Apparel Manufacturing, General Retail Merchandising, Footwear Manufacturing and Retailing and Furniture and Home Furnishings. In the second and fourth quarters of fiscal 1989, the company announced it would sell its Apparel Manufacturing and General Retail Merchandising Groups, respectively, and in accordance with Accounting Principles Board Opinion No. 30, these two segments were thereafter reported as discontinued operations. In addition, during fiscal 1990, the company sold Ethan Allen Inc. from its Furniture and Home Furnishings Group, and a significant part of Senack Shoes, Inc. from its Footwear Manufacturing and Retailing Group. Upon completion of the restructuring program, the company intends to retain four core operations consisting of Converse and Florsheim in the footwear segment, and Broyhill and Lane in the furniture segment. For management discussion and analysis purposes, management believes it would be more informative to concentrate on these core operations.

Net Sales

Net sales of the core companies for fiscal 1990 were $1.47 billion, a decrease of 6.4% from the $1.57 billion last year. Net sales for fiscal 1989 were the same as the $1.57 billion in fiscal 1988. For fiscal 1990, sales for the footwear core companies declined $114.9 million from the prior year, which showed a modest increase over fiscal 1988. The decrease in footwear sales reflects, to a major extent, the consolidation of the International Shoe Company into Florsheim and other restructurings at Florsheim during fiscal 1990, and a decline in sales at Converse due mainly to a softening in demand for fashion canvas footwear, both in the United States and overseas. The furniture core companies sales increased 1.8% over fiscal 1989, which were about even with the prior year.

Net sales of the core companies by segment for the last three fiscal years were as follows, in millions:

Segment	**Fiscal 1990**	Fiscal 1989	Fiscal 1988
Footwear	**$ 674.6**	$ 789.5	$ 783.2
Furniture	**799.5**	785.3	789.1
Total	**$1,474.1**	$1,574.8	$1,572.3

Other Income, Net

Other income for fiscal 1990 was $111.3 million, an increase of $92.4 million from the prior year, which was up slightly from the fiscal 1988 level. The increase in fiscal 1990 was due primarily to the gain on the sale of Ethan Allen Inc., a part of Senack Shoes, Inc. and certain other corporate assets. Proceeds from these sales amounted to $398.5 million before income taxes, with net after-tax proceeds used to reduce long-term debt.

Gross Margins

Gross margins of the core companies for fiscal 1990 were $482.9 million, or 32.8% of net sales, as compared to $502.3 million, or 31.9% of net sales and $540.3 million, or 34.4% of net sales for fiscal 1989 and 1988, respectively. Fiscal 1990 margins of the core companies were favorably affected by the cost reduction and operating efficiencies program implemented as part of INTERCO's restructuring program. This was partially offset by certain promotional pricing actions necessary because of overall soft economic conditions, unfavorable manufacturing variances due to the sales decline in canvas footwear and manufacturing start-up costs within the furniture segment. Margins in fiscal 1989 were adversely impacted by the results of the Footwear Manufacturing and Retailing Group due to promotional costs and unfavorable manufacturing variances resulting from the sales decline in canvas footwear, manufacturing start-up costs within the athletic footwear segment and costs associated with plant closings and realignments within the men's traditional footwear segment. The Furniture and Home Furnishings Group's gross margins were about even with the prior year. For fiscal 1988, the Footwear Manufacturing and Retailing Group showed improved gross margins while the Furniture and Home Furnishings Group's margins were level as a percent of net sales, but up substantially in absolute dollar amount.

Selling, General and Administrative Expenses

Selling, general and administrative expenses of the core companies, including corporate costs and expenses, were $364.6 million, $395.8 million and $377.5 million for fiscal 1990, 1989 and 1988, respectively. As a percent of net sales, selling,

general and administrative expenses were 24.7% for fiscal 1990, as compared to 25.1% for fiscal 1989 and 24.0% for fiscal 1988. Fiscal 1990 reflects a reduction of $31.2 million or 7.9% in the dollar amount of these expenses from year ago levels due to the company's cost reduction and operating efficiencies program, offset somewhat by the decline in sales volume. The increase in fiscal 1989 was primarily attributable to promotional, marketing and realignment costs within the Footwear Manufacturing and Retailing Group.

Operating Earnings

Operating earnings, before corporate and restructuring expenses, interest expense and gain on the sale of assets, were $150.2 million, $177.3 million and $241.3 million for fiscal 1990, 1989 and 1988, respectively. In fiscal 1990, Ethan Allen Inc. and Senack Shoes, Inc. were included through the date of sale as compared with full year earnings in fiscal 1989 and 1988.

For the core companies, operating earnings for fiscal 1990 were $137.7 million, an increase of $10.3 million or 8.1% over the core company operating earnings of $127.4 million for fiscal 1989.

Operating earnings of the core companies by segment for the last two fiscal years were as follows, in millions:

Segment	**Fiscal 1990**	Fiscal 1989
Footwear	**$ 47.0**	$ 38.6
Furniture	**90.7**	88.8
Total	**$137.7**	$127.4

Interest Expense

Interest expense in fiscal 1990 totaled $303.1 million, compared to $141.7 million in fiscal 1989 and $29.2 million in fiscal 1988.

Fiscal 1990 included interest expense related to the restructuring program for the entire year and consisted of $164.0 million related to the Secured Credit Agreement and the medium term notes, $133.7 million on the debentures and miscellaneous interest expense of $5.4 million. Cash interest paid totaled $218.0 million in fiscal 1990.

The increase in fiscal 1989 was attributable to $104.1 million in interest expense related to the restructuring program and interest on the $200.0 million of medium term notes issued in the fourth quarter of the prior year.

Restructuring Expenses

In the third quarter of fiscal 1989, a one-time charge of $14.0 million for restructuring expenses, which was nondeductible for income tax purposes, was incurred.

Earnings (Loss) From Continuing Operations Before Income Taxes

Earnings (loss) from continuing operations were $(58.6) million, as compared to $15.7 million and $198.7 million in fiscal 1989 and 1988, respectively. Earnings were adversely impacted by interest expense and other costs incurred in the company's restructuring program, in addition to the operating and realignment costs and expenses noted above.

Income Taxes

In fiscal 1990, an income tax recovery of $7.7 million was recorded at an effective tax rate of 13.1%. The effective tax rate was adversely affected by provisions for foreign, state and local income taxes and higher gains on asset dispositions for tax purposes than for financial reporting purposes. Income taxes in fiscal 1989 were $20.0 million and exceeded earnings from continuing operations before income taxes due to nondeductible expenses incurred, including the restructuring expenses. For fiscal 1988 the effective tax rate was 42.9%.

The Financial Accounting Standards Board issued Statement No. 96 "Accounting for Income Taxes" in December 1987. This statement requires an asset and liability approach to accounting for deferred income taxes. Initial adoption of this pronouncement may be done on either a prospective or retroactive basis. In December 1989, the Financial Accounting Standards Board issued Statement No. 103 which deferred the required implementation date for this new statement until the company's first quarter of fiscal 1993. Management is of the opinion the adoption of these new accounting regulations will not have a material impact on the company's consolidated financial statements.

Discontinued Operations

Net earnings from discontinued operations were $86.1 million, $74.4 million and $31.6 million in fiscal 1990, 1989 and 1988, respectively. Included in discontinued operations are the results of operations of the Apparel Manufacturing and General Retail Merchandising Groups as well as the net gain realized in fiscal 1990 from the sale of Big Yank Corporation, Cowden Manufacturing Company, Central Hardware Company, International Hat Company, Golde's Department Stores, Inc., Fine's Men's Shops, Incorporated, United Shirt Distributors, Inc. and Stuffed Shirt Inc. amounting to $119.4 million before income taxes and $74.6 million after taxes. In fiscal 1989, the net gain from the sale of assets amounted to $61.9 million before income taxes and $33.9 million after taxes and included goodwill charges related to the two groups, as well as the gain recognized on the sale of Londontown Corporation and other assets. Proceeds from the disposal of these operations ap-

proximated $338.0 million in fiscal 1990 and $220.0 million in fiscal 1989 before income taxes, with net after-tax proceeds used to reduce long-term debt.

Management anticipates disposal of the remaining discontinued operations will be substantially completed during fiscal 1991, with net after-tax proceeds used to further reduce long-term debt. Additional information is contained in Note 3 to the Consolidated Financial Statements.

Earnings (Loss) Per Share

The earnings (loss) per share from continuing operations were $(3.37) and $(0.42) in fiscal 1990 and 1989, respectively, as compared to $2.74 in fiscal 1988. Earnings (loss) per share, including discontinued operations, were $(1.22), $1.53 and $3.50 in fiscal 1990, 1989 and 1988, respectively.

Earnings (loss) per share in fiscal 1990 and 1989 were reduced by Series E Preferred Stock dividend requirements of $83.8 million and $11.8 million, respectively.

Average shares used in the calculation of earnings (loss) per share were 39,998,000 in fiscal 1990, 38,262,000 in fiscal 1989 and 41,456,000 in fiscal 1988.

FINANCIAL CONDITION

Working Capital

Working capital, the relationship between current assets and current liabilities, was $(1,255.7) million at the end of fiscal 1990 as compared to $451.6 million in fiscal 1989 and $986.0 million in fiscal 1988. The current ratio was 0.4 to 1, 1.6 to 1 and 4.7 to 1 in fiscal 1990, 1989 and 1988, respectively. The decrease in working capital and the current ratio at the end of fiscal 1990 was due principally to the reclassification of long-term debt and debentures as current liabilities, as described more fully in the following section. The decrease in working capital and the current ratio at the end of fiscal 1989 was due to the inclusion of $499.8 million of current maturities of long-term debt generated in the recapitalization.

Financing Arrangements

In fiscal 1989, the company replaced its existing revolving credit facilities with a new Secured Credit Agreement. This agreement, which is more fully detailed in Note 7 to the Consolidated Financial Statements, provided the financing for the cash portion of the special dividends paid to shareholders under the company's recapitalization. The company also issued three classes of debentures having a total face value of approximately $1.0 billion.

Of the debentures issued, the Senior Subordinated Debentures are the only debentures that currently require cash interest payments. The Subordinated Discount Debentures require cash interest payments commencing June 15, 1992. The Junior Pay-in-Kind Subordinated Debentures require cash interest payments commencing June 15, 1994.

The Secured Credit Agreement, in addition to providing for periodic cash interest payments, also requires principal payments according to specific amortization and maturity dates, depending on the particular loan tranche. The Asset Sale Bridge Facility requires final payment by no later than May 7, 1990 (however, a waiver has been received extending the payment date to October 1, 1990); the Term Loan/Mortgage Bridge Facility contains various payment requirements with an amortization schedule which began in November 1989 and a final maturity of November 7, 1993; the Borrowing Base Facility has a maturity date of November 7, 1993; and the Seasonal Working Capital Facility contains a final maturity date of November 7, 1991.

In addition to its discontinued operations held for sale, the company is also attempting to sell certain operations and assets included in the Footwear Manufacturing and Retailing Group. Net proceeds from these sales will be used to reduce long-term debt. The company has advised its bank group that because of prevailing economic and market conditions, the proceeds of the company's asset sales will not be sufficient to meet the May 7, 1990 maturity date for the Asset Sale Bridge Facility. At May 6, 1990, the shortfall was approximately $226 million. Further, due to unfavorable market conditions, the company has not mortgaged any of its real estate assets and will not meet the $75 million payment required under the Term Loan/Mortgage Bridge Facility, which amount is also due May 7, 1990, and will not make the June 15 interest payments on the Senior Subordinated Debentures and the Junior Pay-in-Kind Subordinated Debentures.

Under the Secured Credit Agreement, the company is required to satisfy certain financial tests, including minimum net worth, cash coverage, interest coverage and leverage ratio covenants. The company has not been in compliance with certain of these covenants since November 30, 1989, but has been granted waivers by the bank syndicate covering all periods-ending through May 6, 1990.

On May 4, 1990 the company received a temporary waiver from the bank syndicate on its Secured Credit Agreement. The waiver extends the date for certain principal payments from May 7,

1990 to October 1, 1990, provided that such principal payments will become immediately due and payable if the company makes any cash payments in respect of its outstanding debentures. The waiver also waives compliance with certain financial covenants under the agreement and modifies the allocation of the company's credit availability under its Seasonal Working Capital Facility.

As indicated in Note 2 to the Consolidated Financial Statements, the company is negotiating with its lenders to amend its existing Secured Credit Agreement. These proposed amendments contemplate a reconfigured loan structure, extended maturities and revised financial covenants, among other revisions. If the Secured Credit Agreement is not amended prior to October 1, 1990, the company will be unable to make the required principal payments and comply with certain financial covenants of the agreement, which will permit the bank syndicate to accelerate the due dates of the debt. The majority of the long-term debt and debenture agreements of the company contain cross-acceleration clauses which will permit the majority of the lenders and debenture holders to accelerate the due dates of substantially all of the company's debt and debentures. Though no demand for acceleration of the maturity of long-term debt or debentures has occurred, demand can be made should the expected defaults described above occur. Accordingly, the related debt and debentures have been reclassified as current liabilities as of February 24, 1990.

In addition to amending the Secured Credit Agreement, the company is also proposing an exchange of the outstanding Senior Subordinated Debentures for newly issued shares of common stock and new debentures with a lower interest rate, and the exchange of the other series' of debentures and the company's outstanding preferred stock for newly issued shares of common stock. This exchange, if accomplished, would substantially reduce the company's future interest requirements and reduce the company's current debt levels. The company anticipates formalizing the exchange offers to the debenture holders and preferred shareholders before the end of fiscal 1991.

Management believes the proposed restructuring will alleviate the company's liquidity problems and avoid the need to file for bankruptcy. The amendment to the Secured Credit Agreement requires the unanimous approval of the bank syndicate. The exchange offers require acceptance by the holders of at least 90% of the outstanding principal amount of each series of the outstanding debentures and the consent of the requisite number of holders of the common stock and the preferred stock.

Certain divisions and subsidiaries of the company are or have been participants in an underfunded multi-employer pension plan. Because of the disposition of companies in the Apparel Manufacturing Group, the company could be required to contribute to the plan a portion of the funding deficiency. The company has received from the pension fund a written estimate that the company's contribution could be as much as $23.3 million. The company has initiated discussions with the trustees of the plan to determine the timing and amount of the company's required contribution and alternative methods of dealing with such potential liability in light of the company's financial condition. Management does not believe that the amount of any contribution which will ultimately be required from the company will have a material adverse effect on the consolidated financial condition of the company and its subsidiaries.

Capital Expenditures

Capital expenditures in fiscal 1990 were $29.7 million as compared to $53.8 million in fiscal 1989. Depreciation expense was $34.0 million as compared to $40.0 million in fiscal 1989. For fiscal 1991, capital expenditures of the core companies are projected to be approximately $30.0 million.

Dividends

During fiscal 1990, the company did not pay dividends on its Common, Series D Preferred or Series E Preferred Stock. Dividend arrearage on the Series D Preferred Stock at February 24, 1990 was $91 thousand. No dividends will be paid on the company's common shares in the foreseeable future.

Dividend payments on the Series E Preferred Stock are payable in cash, or prior to December 15, 1994 in Series E Preferred Stock, and if not paid in cash or stock, the Aggregate Liquidation Preference increases 4.375% quarterly. Since dividends were not declared, the Liquidation Preference increased 18.68%, or $62.0 million during fiscal 1990.

The company paid regular cash dividends of $31.1 million on the common stock and $1.9 million on the Series D Preferred Stock during fiscal 1989. In addition, in connection with the 1988 recapitalization, the company distributed cash dividends of $1,422.2 million and noncash dividends of $1,003.1 million representing the debentures and the Series E Preferred Stock. The company also paid $0.9 million in fiscal 1989 to redeem its common stock purchase rights.

INTERCO
Consolidated Financial Statements

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Consolidated Balance Sheet

(Dollars in thousands except per share data)

Assets	February 24, 1990	February 25, 1989	February 29, 1988
Current assets:			
Cash	$ 20,642	$ 16,308	$ 12,476
Short-term investments	27,687	61,317	10,823
Receivables, less allowances of $6,153 ($10,599 in 1989 and $10,606 in 1988)	296,546	329,299	310,053
Inventories	347,555	490,967	514,193
Prepaid expenses and other current assets	44,775	41,625	24,984
Net current assets of discontinued operations held for sale	87,735	248,361	382,742
Total current assets	824,940	1,187,877	1,255,271
Net noncurrent assets of discontinued operations held for sale	27,112	98,011	138,902
Property, plant and equipment:			
Land	8,728	19,105	18,454
Buildings and improvements	192,651	321,591	297,876
Machinery and equipment	223,037	257,043	252,281
	424,416	597,739	568,611
Less accumulated depreciation	237,497	270,669	251,373
Net property, plant and equipment	186,919	327,070	317,238
Other assets	109,339	162,344	118,989
	$1,148,310	$1,775,302	$1,830,400

See accompanying notes to consolidated financial statements.

Liabilities and Shareholders' Equity (Deficit)	**February 24, 1990**	February 25, 1989	February 29, 1988
Current liabilities:			
Notes payable	**$ 3,444**	$ 6,017	$ 70,517
Current maturities of long-term debt	**386,630**	509,961	4,816
Long-term debt and debentures classified as current (notes 7 and 8)	**1,492,587**	–	–
Accounts payable	**89,186**	99,231	105,165
Accrued employee compensation	**20,747**	27,317	33,021
Accrued interest expense	**17,395**	35,339	3,568
Other accrued expenses	**51,912**	53,618	35,622
Income taxes	**18,735**	4,785	16,606
Total current liabilities	**2,080,636**	736,268	269,315
Long-term debt, less current maturities	**3,176**	1,178,180	266,191
Debentures	**–**	808,657	–
Other long-term liabilities	**31,066**	57,947	43,557
Shareholders' equity (deficit):			
Preferred stock, authorized 10,000,000 shares:			
Series D, no par value—issued 11,743 shares in 1990, 19,103 shares in 1989 and 571,133 shares in 1988	**1,174**	1,910	57,113
Series E, $1.00 stated value—issued 3,320,702 shares with an aggregate liquidation preference of $394,108 and $332,070 at February 24, 1990 and February 25, 1989, respectively	**3,321**	3,321	–
Common stock, $3.75 stated value, authorized 150,000,000 shares—issued 38,708,606 shares in 1990 and 41,356,847 shares in 1989 and 1988	**145,157**	155,088	155,088
Paid-in capital	**57,772**	179,337	44,539
Retained earnings (deficit)	**(1,173,992)**	(1,208,250)	1,179,964
	(966,568)	(868,594)	1,436,704
Less common stock in treasury, at cost (3,493,812 and 5,173,811 shares in 1989 and 1988, respectively)	**–**	137,156	185,367
Total shareholders' equity (deficit)	**(966,568)**	(1,005,750)	1,251,337
	$ 1,148,310	$ 1,775,302	$1,830,400

Consolidated Statement of Earnings

(Dollars in thousands except per share data)

Years Ended	**February 24, 1990**	February 25, 1989	February 29, 1988
Income:			
Net sales	**$1,656,079**	$2,011,962	$1,995,974
Other income, net	**111,282**	18,943	13,714
	1,767,361	2,030,905	2,009,688
Costs and expenses:			
Cost of sales	**1,097,558**	1,335,678	1,288,748
Selling, general and administrative expenses	**425,246**	523,797	493,015
Interest expense	**303,123**	141,735	29,188
Nondeductible restructuring expenses	**—**	14,000	—
	1,825,927	2,015,210	1,810,951
Earnings (loss) from continuing operations before income taxes	**(58,566)**	15,695	198,737
Income taxes	**(7,691)**	19,977	85,303
Net earnings (loss) from continuing operations	**(50,875)**	(4,282)	113,434
Discontinued operations (net of taxes of $49,765 in 1990, $55,047 in 1989 and $23,154 in 1988)	**86,082**	74,432	31,569
Net earnings	**35,207**	70,150	145,003
Less—preferred stock dividend requirements	**(83,838)**	(11,784)	—
Net earnings (loss) applicable to common stock	**$ (48,631)**	$ 58,366	$ 145,003
Earnings (loss) per common share:			
Continuing operations	**$(3.37)**	$(0.42)	$2.74
Net earnings (loss)	**$(1.22)**	$ 1.53	$3.50

See accompanying notes to consolidated financial statements.

Consolidated Statement of Cash Flows

(Dollars in thousands)

Years Ended	February 24, 1990	February 25, 1989
Cash Flows from Operating Activities:		
Net loss from continuing operations	$ (50,875)	$ (4,282)
Adjustments to reconcile net loss to net cash provided (used) by operating activities:		
Gain on disposal of assets	(101,920)	—
Noncash interest expense	102,581	30,884
Depreciation of property, plant and equipment	33,980	40,037
Amortization of intangible assets and other noncash charges	6,987	3,280
Decrease in deferred income taxes	(15,785)	(12,955)
Net decrease in deferred items	(7,735)	(45,439)
Increase (decrease) in accounts payable and accrued expenses	(25,820)	38,084
Increase in accounts receivable	(12,654)	(19,246)
Decrease in inventories	19,477	23,226
Increase in prepaid expenses and other assets	(8,052)	(1,228)
Increase (decrease) in income taxes payable	13,372	(11,821)
Net cash provided (used) by operating activities of continuing operations	(46,444)	40,540
Net cash provided by discontinued operations	317,607	249,704
Net cash provided by operating activities	271,163	290,244
Cash Flows from Investing Activities:		
Net cash proceeds from the disposal of assets	398,483	4,134
Additions to property, plant, equipment and leasehold interests	(29,663)	(50,966)
Net cash provided (used) by investing activities	368,820	(46,832)
Cash Flows from Financing Activities:		
Proceeds from the sale or issuance of common stock	4,924	19,994
Payments to acquire treasury stock	—	(102,341)
Dividends paid	—	(1,456,162)
Proceeds from issuance of long-term debt	175,043	1,967,500
Reduction of long-term debt and notes payable	(849,246)	(617,401)
Other	—	(676)
Net cash used in financing activities	(669,279)	(189,086)
Net increase (decrease) in cash and cash equivalents	(29,296)	54,326
Cash and cash equivalents at beginning of year	77,625	23,299
Cash and cash equivalents at end of year	$ 48,329	$ 77,625
Supplemental disclosure:		
Cash payments for income taxes	$ 40,169	$ 52,067
Cash payments for interest, net of amounts capitalized	$ 218,042	$ 73,926

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Financial Position

(Dollars in thousands)

Year Ended	February 29, 1988
Working capital provided by:	
Net earnings	$145,003
Items not affecting working capital:	
Depreciation	40,570
Other, net	8,750
Operations	194,323
Disposal of property, plant and equipment	1,145
Issuance of common stock	4,606
Additions to long-term debt	205,533
Change in net noncurrent assets of discontinued operations held for sale	4,956
Other, net	252
	410,815
Working capital used for:	
Cash dividends	64,219
Additions to property, plant and equipment	45,925
Reduction of long-term debt	82,700
Purchase of common treasury shares	152,255
Retirement of preferred stock	6,266
Conversion of preferred stock	1,921
	353,286
Increase in working capital	$ 57,529
Working capital increased (decreased) by:	
Cash and short-term investments	$ (49,285)
Receivables	45,595
Inventories	81,399
Prepaid expenses and other current assets	8,680
Change in net current assets of discontinued operations held for sale	8,350
Notes payable	(1,677)
Current maturities of long-term debt	2,870
Accounts payable and accrued expenses	(38,560)
Income taxes	157
	$ 57,529

See accompanying notes to consolidated financial statements.

Consolidated Statement of Shareholders' Equity (Deficit)

(Dollars in thousands except per share data)

	Preferred Stock		Common Stock		Paid-in	Retained Earnings	
	Series D	Series E	Issued	Treasury	Capital	(Deficit)	Total
Balance February 28, 1987	$ 61,795	$ —	$163,643	$ (96,475)	$ 98,246	$ 1,099,006	$ 1,326,215
Net earnings						145,003	145,003
Cash dividends:							
Preferred stock						(4,621)	(4,621)
Common stock—$1.60						(59,598)	(59,598)
Retirement of capital stock:							
Preferred—27,605 shares	(2,761)				(3,505)		(6,266)
Common—2,457,728 shares			(9,216)	63,315	(54,099)		—
Conversion of preferred stock:							
Series D—19,208 shares	(1,921)		311		1,609		(1)
Issuance of common stock:							
Options—93,321 shares			350	48	2,288		2,686
Purchase of 4,166,582 shares				(152,255)			(152,255)
Foreign currency translations						174	174
Balance February 29, 1988	57,113	—	155,088	(185,367)	44,539	1,179,964	1,251,337
Net earnings						70,150	70,150
Cash dividends:							
Preferred stock						(1,944)	(1,944)
Common stock—$0.86						(31,086)	(31,086)
Common stock rights—$0.025						(875)	(875)
Special cash—$38.60						(1,422,257)	(1,422,257)
Securities dividends:							
Debentures—$21.66						(789,657)	(789,657)
Preferred stock—$5.79		3,321			210,160	(213,481)	—
Retirement of capital stock:							
Common—3,900,549 shares			(14,627)	150,552	(135,925)		—
Conversion of preferred stock:							
Series D—552,030 shares	(55,203)		11,388		43,808		(7)
Issuance of common stock:							
Options—564,820 shares			2,118		15,735		17,853
Restricted stock—299,011 shares			1,121		1,020		2,141
Purchase of 2,220,550 shares				(102,341)			(102,341)
Foreign currency translations						936	936
Balance February 25, 1989	1,910	3,321	155,088	(137,156)	179,337	(1,208,250)	(1,005,750)
Net earnings						35,207	35,207
Retirement of capital stock:							
Common—3,493,812 shares			(13,102)	137,156	(124,054)		—
Conversion of preferred stock:							
Series D—7,360 shares	(736)		2,512		(1,776)		—
Issuance of common stock:							
Options—159,040 shares			596		(302)		294
Restricted stock—16,764 shares			63		4,567		4,630
Foreign currency translations						(949)	(949)
Balance February 24, 1990	$ 1,174	$3,321	$145,157	$ —	$ 57,772	$(1,173,992)	$ (966,568)

See accompanying notes to consolidated financial statements.

(Dollars in thousands except per share data)

1. SIGNIFICANT ACCOUNTING POLICIES

The company and its subsidiaries follow generally accepted accounting principles to present fairly their consolidated financial position, results of operations, cash flows and changes in financial position. The major accounting policies of the company are set forth below.

Principles of Consolidation — The consolidated financial statements include the accounts of the company and all its subsidiaries, the majority of which are wholly owned. All material intercompany transactions have been eliminated in consolidation.

Fiscal Year — In fiscal 1989, the company changed its fiscal year to end on the last Saturday in February. The company's fiscal year ended on the last day of February for fiscal 1988.

Statement of Cash Flows — In November 1987, the Financial Accounting Standards Board (FASB) issued Statement No. 95 "Statement of Cash Flows." The company adopted the provisions of Statement No. 95 in fiscal 1989 and elected not to restate the statement of changes in financial position presented for fiscal year 1988. For purposes of the statement of cash flows, the company considers all short-term investments with a maturity at date of purchase of three months or less to be cash equivalents.

Inventories — Inventories are stated at the lower of cost (first-in, first-out) or market, except for certain footwear manufacturing inventories which are valued on the "last-in, first-out" method of inventory valuation.

Property, Plant and Equipment — Property, plant and equipment are stated at cost. Expenditures for improvements are capitalized, while normal repairs and maintenance are expensed as incurred. When properties are retired or otherwise disposed of, the related cost and accumulated depreciation or amortization are removed from the accounts and gains or losses on the dispositions are reflected in results of operations. For financial reporting purposes, the company utilizes both accelerated and straight-line methods of computing depreciation and amortization. Such expense is computed based on the estimated useful lives of the respective assets, which generally range from 15 to 40 years for buildings and improvements, and from 3 to 20 years for machinery and equipment. Approximately 70% of depreciation and amortization expense was computed using the straight-line method in each fiscal year presented.

Excess of Cost Over Fair Value of Net Assets Acquired — The excess of cost over fair value of net assets of companies acquired is included in other assets and is generally amortized on a straight-line basis, over periods ranging from 25 to 40 years.

Income Taxes — Deferred income taxes are provided on transactions which are reported for financial reporting purposes in different periods than for income tax reporting purposes. It is the company's intent that the undistributed earnings of its subsidiaries will either be reinvested in the subsidiaries or distributed tax-free to the parent company. Generally, no provision has been made for income taxes on such undistributed earnings.

The FASB issued Statement No. 96 "Accounting for Income Taxes," in December 1987. This statement requires an asset and liability approach to accounting for deferred income taxes. Initial adoption of this pronouncement may be done on either a prospective or retroactive basis. In December 1989, the FASB issued Statement No. 103 which deferred the required implementation date for this new statement until the company's first quarter of fiscal 1993. Management is of the opinion the adoption of these new accounting regulations will not have a material impact on the consolidated financial statements.

Earnings Per Share — Earnings per share are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the year, plus those common shares which would have been issued if conversion of all Series D Preferred Stock had taken place at the beginning of each period. Stock options, the exercise of which would result in dilution of earnings per share, are considered common stock equivalents. Net earnings for these computations are reduced by the dividend requirements of the Series E Preferred Stock.

Reclassification — Certain fiscal 1989 and 1988 amounts have been reclassified to conform to the fiscal 1990 presentation.

2. PROPOSED RESTRUCTURING

As a result of a recapitalization plan adopted in fiscal 1989, the company distributed to holders of its common stock $1.42 billion in cash, approximately $1.0 billion face amount of debentures and 3,320,702 shares of its Series E Preferred Stock. The recapitalization immediately changed the company's capital structure to one that is highly leveraged. To meet the interest expense and principal repayment obligations of the indebtedness incurred in connection with the recapitalization, the company embarked on a program to lower its cost structure and streamline its business to allow senior management to focus its attention on four core companies, Broyhill Furniture Industries, Inc., The Lane Company, Incorporated, The Florsheim Shoe Company and Converse Inc., and to sell its non-core businesses and certain other assets to repay certain of its debt obligations.

Because of prevailing economic and market conditions, the company's asset sales have not occurred as rapidly as expected and the proceeds from the company's asset sales have been below projected amounts. In addition, operating results have been lower than anticipated, particularly in the Footwear Manufacturing and Retailing Group. As a result, the company must currently service substantially more debt than was originally anticipated. The company will not have sufficient resources to make the required principal payments on its bank debt due October 1, 1990, as extended by waiver from the original May 7, 1990 due date, and expects not to be in compliance with certain financial covenants of the Secured Credit Agreement. Further, it is likely the company will not have sufficient resources to make principal payments on certain senior debt securities which come due in the next few years and will be unable to service its increasing debt and preferred stock dividend obligations arising from the pay-in-kind features of certain of the securities issued in connection with the recapitalization.

The company is seeking to implement a restructuring plan to achieve changes in the company's debt and capital structure to alleviate these problems and avoid the necessity of filing for bankruptcy. As part of the restructuring plan, the company proposes to amend its Secured Credit Agreement by extending the contractual maturities, including the October 1, 1990 principal payments, revising the financial covenants and reconfiguring the loan structure, among other revisions. The proposed Amended Secured Credit Agreement would also provide an available credit facility to repay other debt which comes due in the future. In addition, the company is also proposing an exchange of the company's Senior Subordinated Debentures for newly issued common stock and new debentures with a lower interest rate, and the exchange of the other series' of debentures and the company's outstanding preferred stock for newly-issued common stock.

The amendment to the Secured Credit Agreement requires the unanimous approval of the bank syndicate. The exchange offers require acceptance by the holders of at least 90% of the outstanding principal amount of each series of the outstanding debentures; the conversion of the preferred stock into common stock requires the consent of the requisite number of holders of the common stock and the preferred stock.

3. DISCONTINUED OPERATIONS

In fiscal 1989, the company announced its intent to offer for sale the Apparel Manufacturing Group and the General Retail Merchandising Group. In accordance with Accounting Principles Board Opinion No. 30, the financial results for the groups are reported as "Discontinued Operations" and results from prior periods have been restated. Condensed results of the discontinued operations were as follows:

	1990	1989	1988
Net sales	**$568,406**	$1,265,789	$1,345,449
Earnings before income taxes	**16,493**	67,543	54,723
Income taxes	**5,013**	27,047	23,154
Net earnings	**11,480**	40,496	31,569
Gain on disposal (net of income tax of $44,752 and $28,000 for 1990 and 1989, respectively)	**$ 74,602**	$ 33,936	$ —
Accounts receivable, net	**$ 45,913**	$ 122,737	$ 176,603
Inventories	**74,316**	205,531	290,901
Other current assets	**10,667**	17,615	19,265
Total current assets	**130,896**	345,883	486,769
Current liabilities	**43,161**	97,522	104,027
Net current assets	**$ 87,735**	$ 248,361	$ 382,742
Property, plant and equipment, net	**$ 28,707**	$ 139,531	$ 162,261
Other assets	**7,026**	4,061	27,799
Total	**35,733**	143,592	190,060
Long-term liabilities	**8,621**	45,581	51,158
Net noncurrent assets	**$ 27,112**	$ 98,011	$ 138,902

In fiscal 1990, the company disposed of its Central Hardware Company, Big Yank Corporation, Cowden Manufacturing Company, Fine's Men's Shops, Incorporated, United Shirt Distributors, Inc., Stuffed Shirt Inc., International Hat Company and Golde's Department Stores, Inc. subsidiaries, plus certain real estate, for approximately $338,000 in cash (net of commissions). The net gains and losses recognized on these disposals are reflected in the Consolidated Statement of Earnings for fiscal 1990.

In fiscal 1989, the company completed the sale of its Londontown Corporation subsidiary for $178,000 in cash and sold the assets, net of liabilities, of The Biltwell Company, Inc. for approximately $42,000 in cash. The gains recognized on these sales are reflected in the Consolidated Statement of Earnings for fiscal 1989 along with the write-off of $20,564 in goodwill, which was associated mainly with the Apparel Manufacturing Group and was nondeductible for income tax purposes.

Management anticipates that disposal of the remaining companies in the Apparel Manufacturing and General Retail Merchandising Groups will be substantially completed during fiscal 1991.

4. GAIN ON DISPOSAL OF ASSETS

On June 29, 1989, the company sold its Ethan Allen Inc. subsidiary for approximately $388,000 consisting of $357,000 in cash, certain real estate assets and the assumption of $23,500 of existing debt and capitalized leases. In addition to the $388,000, the company received warrants to purchase up to 8% of the common stock of the purchaser. Additionally, on September 18, 1989, the company sold certain furniture, fixtures and inventories of its Senack Shoes, Inc. subsidiary for approximately $36,300 in cash. The net gain of $101,920 recognized on these sales, and sales of certain other corporate assets, are included in Other Income, Net in the Consolidated Statement of Earnings for fiscal 1990.

5. INVENTORIES

Inventories are summarized as follows:

	1990	1989	1988
Retail merchandise	**$ 83,079**	$129,723	$137,499
Finished products	**164,333**	216,739	225,337
Work-in-process	**40,359**	52,167	51,653
Raw materials	**59,784**	92,338	99,704
	$347,555	$490,967	$514,193

All of the major categories of inventory, except retail merchandise, include certain items valued on the "last-in, first-out" (LIFO) method. Had the "first-in, first-out" (FIFO) method been applied to all inventories, they would have been stated at approximately $363,082, $511,325 and $537,146 at fiscal years ended 1990, 1989 and 1988, respectively.

In fiscal 1990, certain footwear manufacturing inventories were reduced resulting in a liquidation of the related LIFO reserves. The effect of this liquidation resulted in a decrease in loss from continuing operations before income taxes of approximately $5,000.

6. LINES OF CREDIT

The company's prior revolving credit facilities, enabling it to borrow up to $200,000 from several U.S. and foreign banks under various borrowing options, were replaced in fiscal 1989 by the Secured Credit Agreement.

Average short-term borrowings outstanding on these facilities during fiscal 1989 and 1988 were $208,000 and $123,000, respectively, with a weighted average interest rate thereon of 7.8% and 7.1%, respectively. Maximum short-term borrowings at any month-end were $290,500 and $172,500 in fiscal years 1989 and 1988, respectively.

7. LONG-TERM DEBT

Long-term debt consisted of the following:

	1990	1989	1988
Secured Credit Agreement	**$773,493**	$1,424,847	$ –
7.95% to 8.875% promissory notes due 1991 to 1993	**200,000**	200,000	200,000
6.0% to 8.75% industrial revenue bonds payable in varying amounts through 2004	**15,734**	41,352	41,798
Other debt	**—**	11,065	17,537
Capital lease obligations	**1,115**	10,877	11,672
	990,342	1,688,141	271,007
Less current maturities	**386,630**	509,961	4,816
Less amounts classified as current	**600,536**	–	–
	$ 3,176	$1,178,180	$266,191

In fiscal 1989, the company entered into the Secured Credit Agreement with a group of banks. The loans available under the Secured Credit Agreement consisted of a $1,150,000 Asset Sale Bridge Facility, a $265,000 Term Loan/Mortgage Bridge Facility, a $250,000 Borrowing Base Facility and a $250,000 Seasonal Working Capital Facility providing for letters of credit as well as for loans. On November 29, 1988, the company borrowed $1,655,000 to pay the cash portion of the special dividend as part of the company's restructuring plan and to refinance existing debt.

On May 4, 1990, the company received a waiver, effective May 7, 1990, from the bank syndicate on its Secured Credit Agreement. The waiver extends the date for certain principal payments from May 7, 1990 to October 1, 1990, waives compliance with certain financial covenants under the agreement and modifies the allocation of the company's credit availability under its Seasonal Working Capital Facility.

The $244,469 amount outstanding at fiscal year end 1990 under the Asset Sale Bridge Facility is payable by October 1, 1990. The Secured Credit Agreement requires the company to sell stock or assets of the remaining business units, other than the core companies of Converse, Florsheim, Broyhill and Lane, sufficient to fund these mandatory reductions.

The $225,024 outstanding under the Term Loan/Mortgage Bridge Facility at February 24, 1990 consists of $207,354 issued under Primary Commitments and $17,670 issued under Secondary Commitments. The Primary Commitments must be reduced by $75,000 by October 1, 1990, and by 1/17 of the difference between $75,000 and the $225,000 outstanding on December 31, 1988, on each November 7, February 7, May 7 and August 7 from November 7, 1989 to November 7, 1993 (the commitment reduction dates). The Secondary Commitments must be reduced on each commitment reduction date by an amount equal to the then aggregate amount of Secondary Commitments outstanding divided by the number of remaining commitment reduction dates. The Secured Credit Agreement requires the company and its subsidiaries to incur debt secured by mortgages on real property in an amount sufficient to fund the $75,000 reduction of the Primary Commitments by October 1, 1990. The Term Loan/Mortgage Bridge Facility matures on November 7, 1993.

The Borrowing Base Facility matures on November 7, 1993, and the Seasonal Working Capital Facility matures on November 7, 1991. Total borrowings outstanding under the Borrowing Base Facility were $239,000 and $175,000 at February 24, 1990 and February 25, 1989, respectively. Total borrowings outstanding under the Seasonal Working Capital Facility were $65,000 and $20,000 at February 24, 1990 and February 25, 1989, respectively. Aggregate loans outstanding under these facilities may not exceed the "Borrowing Base," as defined by the Secured Credit Agreement. The Borrowing Base is computed by reference to the amount of inventory and accounts receivable of the company and certain subsidiaries, plus a dollar amount established under the agreement. At February 24, 1990 the Borrowing Base was $357,285.

On the earlier of October 1, 1990 or the date the company sells its Apparel Manufacturing Group, total availability under the Seasonal Working Capital Facility will be reduced from $250,000 to $200,000. No more than $45,000 in stand-by letters of credit, or $135,000 in trade letters of credit may be outstanding at any time. In addition, the aggregate principal amount of loans outstanding under the Seasonal Working Capital Facility may not exceed (i) $115,000 at any time, or (ii) $75,000 for a period of at least 30 consecutive days during the period from January 1 through February 28 of each year.

The borrowings and other extensions of credit under the Secured Credit Agreement are unconditionally guaranteed by each wholly-owned active domestic subsidiary of the company, such guarantees being limited to the maximum amount which will not result in a violation of creditors' rights under relevant principles of law. Such borrowings and the guarantees thereof are secured by (i) mortgages or deeds of trust on certain real property owned by the company and its subsidiaries, (ii) patent and trademark security agreements covering patents and trademarks owned by the company and its subsidiaries, (iii) security interests in inventories, accounts receivable, equipment and other personal property of the company and its subsidiaries, and (iv) pledges of the stock of active domestic subsidiaries of the company. Under the Secured Credit Agreement, the banks also have the right to require (to the extent permitted under the then-existing agreements) that real or personal property of the company or any active domestic subsidiary not at the time subject to a lien or security interest in favor of the banks be subjected to such a lien and that active domestic subsidiaries, the stock of which is not at the time pledged to the banks, be so pledged.

The outstanding borrowings under the Secured Credit Agreement bear interest at the company's option at either prime rate plus 1½% or adjusted LIBOR plus 2½%. At February 24, 1990 the interest rate for the borrowings under this agreement was 11.50%, and there were no borrowings issued under the LIBOR option.

The company is required to pay a commitment fee of ½ of 1% per annum on the average daily amount of the commitments of the banks, less the average daily amount of loans outstanding, payable quarterly in arrears until such commitments are terminated. The principal amount of the commitments, upon which the commitment fee was calculated, was $167,478 at February 24, 1990. The company also pays an annual agency fee of $400 and certain other fees and expenses in connection with the Secured Credit Agreement.

In addition, a fee of 2½% per annum on the daily average available amount under each letter of credit is assessed for the account of the lenders ratably; a further fee of not more than ¼ of 1% per annum on the daily average available amount under each letter of credit and a customary administrative charge for issuance of the letter of credit are each payable to the relevant issuing bank. Letter of credit fees are payable quarterly in arrears.

Under the Secured Credit Agreement, the company is required to satisfy certain financial tests, including minimum net worth, cash coverage, interest coverage and leverage ratio covenants. The company has not been in compliance with these covenants since November 30, 1989 (except for the leverage ratio test which was not applicable until February 24, 1990) and the bank syndicate has granted temporary waivers in this regard through October 1, 1990. Further, as indicated in Note 2, the company proposes to amend its existing Secured Credit Agreement. These amendments contemplate a reconfigured loan structure, extended maturities and revised financial covenants, among other revisions. If the Secured Credit Agreement is not amended prior to October 1, 1990, the company will be unable to make the required principal payments and comply with certain financial covenants of the agreement, which will permit the bank syndicate to accelerate the due dates of the debt. The majority of the long-term debt agreements of the company contain cross-acceleration clauses which will permit the majority of the lenders to accelerate the due dates of substantially all of the company's debt. Though no demand for acceleration of the maturity of long-term debt has occurred, demand can be made when the expected defaults described above and in Note 8 occur. Accordingly, the related debt has been reclassified as a current liability as of February 24, 1990.

During the fourth quarter of fiscal 1988, the company issued $200,000 of medium term promissory notes with various interest rates and maturity dates. A January 15, 1988 promissory note in the amount of $125,000 with an interest rate of 8.875% matures on January 15, 1993. Three promissory notes in the amount of $25,000 each were issued in February 1988 with interest rates of 7.95%, 8.30% and 8.45%, and with maturity dates of February 5, 1991, February 25, 1992, and February 16, 1993, respectively. The $125,000 promissory note was issued at a discount of $938 and the discount and the costs relating to the issuance of the notes are being amortized over the respective lives of the notes as a charge to interest expense.

Scheduled maturities of long-term debt are $386,630, $131,105, $190,452, $269,450 and $250 for fiscal years 1991 through 1995, respectively.

Included in other assets at February 24, 1990, is $18,735 in unamortized deferred debt costs which are being amortized over the lives of certain debt instruments. Amortization of debt issue costs amounted to $24,722 and $11,043 for fiscal 1990 and 1989, respectively. The majority of these deferred costs relate to the debt incurred in the restructuring.

8. DEBENTURES

The debentures were issued as part of the special dividends declared by the Board of Directors in fiscal 1989 in the restructuring plan and consist of the following, by class of debenture:

	1990	1989
13.75% Senior Subordinated Debentures, net of unamortized original issue discount of $7,295 and $7,967, based on an effective interest rate of 14.1%, due December 15, 2000	**$397,075**	$396,403
14.0% Subordinated Discount Debentures, net of unamortized original issue discount of $111,064 and $158,061, based on an effective interest rate of 16.1%, due December 15, 2003	**275,235**	228,237
14.5% Junior Pay-in-Kind Subordinated Debentures, net of unamortized original issue discount of $24,356 and $22,604, based on an effective interest rate of 15.9%, due December 15, 2003	**212,955**	184,017
	885,265	808,657
Less amounts classified as current	**885,265**	–
	$ –	$808,657

The Senior Subordinated Debentures mature on December 15, 2000, pay interest semiannually at the annual rate of 13.75% and require three annual sinking fund payments of 25% of the principal amount commencing on December 15, 1997 to retire 75% of the debentures prior to final maturity. On or after December 15, 1992, the debentures may be redeemed at the company's option at 108.75% of face value, decreasing to 100% in 1997. The debentures are subordinated in right of payment to all senior debt of the company.

The Subordinated Discount Debentures mature on December 15, 2003, and require three annual sinking fund payments of 25% of the principal amount commencing on December 15, 2000 to retire 75% of the debentures prior to final maturity. Interest on the debentures will accrue commencing December 15, 1991 at the annual rate of 14.0%, and will be payable semiannually with the

first interest payment on June 15, 1992. On or after December 15, 1995, the debentures may be redeemed at the company's option at 108.75% of face value, decreasing to 100% in 2000. The debentures are subordinated in right of payment to all senior debt, including the Senior Subordinated Debentures of the company.

The Junior Pay-in-Kind Subordinated Debentures mature on December 15, 2003. Interest is payable semiannually at the annual rate of 14.5%, and at the option of the company, may be paid in cash or additional debentures until December 15, 1993. Interest payments commenced on June 15, 1989 and both semiannual interest payments required since the commencement date were paid in additional debentures. On or after December 15, 1995, the debentures may be redeemed at the company's option at 109.25% of face value, decreasing to 100% in 2000. The debentures are subordinated in right of payment to all senior debt, including the Senior Subordinated Debentures and the Subordinated Discount Debentures of the company.

As described in Note 7, the company has obtained a waiver on certain provisions of its Secured Credit Agreement through October 1, 1990. The waiver extends the date for certain principal payments from May 7, 1990 to October 1, 1990, provided that such principal payments will become immediately due and payable if the company makes any cash payments on its outstanding debentures. The company will not make the cash interest payments on its Senior Subordinated Debentures due June 15, 1990 and will be in default on July 15, 1990. The Subordinated Discount Debentures and Junior Pay-in-Kind Subordinated Debentures contain cross-acceleration provisions. These defaults will allow the debenture holders to accelerate the due dates of all the outstanding debentures. Though no demand for acceleration has occurred, demand can be made when the expected defaults described above occur. Accordingly, the debentures and $6,786 in accrued interest on the Junior Pay-in-Kind Subordinated Debentures have been reclassified as current liabilities as of February 24, 1990.

As discussed more fully in Note 2, the company is currently contemplating a restructuring which would involve the exchange of the debentures outstanding for newly issued equity and debt securities.

9. PREFERRED STOCK

The company's preferred stock consisted of:

Series D — At fiscal years ended 1990, 1989 and 1988, the outstanding Series D Preferred Stock consisted of 11,743, 19,103 and 571,133 shares, respectively, of $7.75 cumulative convertible with stated and involuntary liquidating value of $100.00 per share.

Each share of the Series D Preferred Stock is convertible into 91.0028 shares (4.3243 prior to restructuring) of the company's common stock. The Series D Preferred Stock may be redeemed, at the company's option, at $103.75 per share in 1990, decreasing to $100.00 per share in 1994, plus accumulated dividends, subject to Delaware corporation law.

Subsequent to February 25, 1989, the Board of Directors was required under Delaware corporation law to omit the quarterly dividend payments of $1.9375 per share on the Series D Preferred Stock. The dividend arrearage on the 11,743 shares outstanding at February 24, 1990 totaled $91.

Series E — The Series E Preferred Stock pays quarterly dividends at an annual rate of 17.5% and had a $100.00 per share initial aggregate liquidation preference. Dividend requirements commenced on March 15, 1989, payable in cash, or prior to December 15, 1994 in Series E Preferred Stock, and if not paid in cash or stock, the aggregate liquidation preference increases 4.375% quarterly. In fiscal 1990, no payments were made in cash or Series E Preferred Stock and, as a result, the aggregate liquidation preference at February 24, 1990 had increased to $394,108.

Each share of Series E Preferred Stock, including the shares represented by depositary receipts, may be redeemed at the company's option at 101% of the then aggregate liquidation preference per share, plus accrued dividends, through December 15, 1994 and at 100% thereafter. The shares are exchangeable, at the company's option, on any dividend date after December 15, 1994, into Junior Subordinated Exchange Debentures which would bear interest at the same rate as the Series E Preferred Stock.

Each share of Series E Preferred Stock, including the shares represented by depositary receipts, carried warrants to purchase 3.5 shares of common stock at $6.25 per share. On March 14, 1989 the warrants separated from the Series E Preferred Stock and warrant certificates evidencing the right to purchase 11,622,457 shares of common stock were issued. The warrants became exercisable on July 1, 1989 and expire on March 15, 1992. Warrants for three shares of common stock were exercised during fiscal year ended February 24, 1990.

As discussed more fully in Note 2, the company is currently contemplating a restructuring which would involve the exchange of the preferred stock outstanding for newly issued equity securities.

10. COMMON STOCK

Shares of common stock were reserved for the following purposes at February 24, 1990:

	Number of Shares
Common stock options:	
Granted	9,534,144
Available for grant	3,007,525
Common stock warrants	11,622,454
Conversion of Series D Preferred Stock	1,068,645
	25,232,768

Under the company's Stock Option Plans, certain key employees may be granted incentive options, nonqualified options, stock appreciation rights or combinations thereof. Options and stock appreciation rights granted under the 1980 and 1985 Plans may not be less than 100% of the fair market value of the common stock on the date of grant. All options which have been granted, incentive or nonqualified, were at 100% of fair market value on the date of grant. Incentive options and nonqualified options expire ten years after the date of grant. At February 24, 1990, no appreciation rights had been granted. Options outstanding and the exercise prices thereon and shares available for grant were adjusted in accordance with anti-dilution provisions of the plans subsequent to the record dates of the fiscal 1989 restructuring dividends.

On June 26, 1989, the shareholders approved the INTERCO INCORPORATED 1989 Stock Option Plan authorizing the granting to key employees, including officers, of nonqualified options to purchase 7,500,000 shares of common stock at 100% of fair market value on the date of grant.

At February 24, 1990, information regarding options granted but not exercised was as follows:

	Option Shares Outstanding	Dates of Grant	Price Range
1977 Plan	86,932	October 7, 1985 - March 10, 1987	$2.2711 - $3.00
1980 Plan	2,723,842	July 10, 1981 - October 31, 1989	$0.97 - $3.5387
1982 Plan	21,300	November 3, 1986	$2.0183
1985 Plan	1,020,070	March 10, 1987 - October 31, 1989	$0.97 - $3.00
1989 Plan	5,682,000	January 23, 1989 - May 8, 1989	$2.50 - $2.9375

Changes in options granted are summarized as follows:

	1990		1989		1988	
	Shares	**Average Price**	Shares	Average Price	Shares	Average Price
Beginning of year	**4,168,134**	**$2.61**	850,312	$32.30	637,120	$27.17
Assumed options of acquired companies	**—**	**—**	—	—	103,488	24.02
Restructuring dividends	**—**	**—**	4,276,147	—	—	—
Granted	**7,067,500**	**2.56**	—	—	284,250	42.94
Exercised	**(159,040)**	**1.68**	(564,820)	25.31	(93,321)	24.67
Cancelled	**(1,542,450)**	**2.86**	(393,505)	5.79	(81,225)	29.75
End of year	**9,534,144**	**2.55**	4,168,134	2.61	850,312	32.30
Exercisable at end of year	**3,234,991**		1,723,975		383,181	

In July 1988, previously issued Common Share Purchase Rights were redeemed for $875. On July 11, 1988 the company declared a dividend of one Common Share Purchase Right for each outstanding share of common stock, effective July 21, 1988. The rights will not be exercisable, or transferable apart from the common stock, until ten days after another person or group of persons acquires 15% or more of the common stock or commences, or announces its intention to commence, a tender or exchange offer for 15% or more of the common stock. Each right entitles its holder to buy one share of common stock at an exercise price of $10.00. In certain circumstances, the rights will entitle their holders to purchase larger amounts of common stock or stock in an acquiring company. In addition to the shares reserved above, an additional 63,941,374 shares have been reserved under this plan.

11. INCOME TAXES

Income taxes were comprised of the following:

	1990	1989	1988
Current:			
Federal	$ (581)	$14,814	$69,999
State and local	6,661	9,403	13,262
Foreign	2,014	2,598	1,716
	8,094	26,815	84,977
Deferred	(15,785)	(6,838)	326
	$ (7,691)	$19,977	$85,303

The following table reconciles the differences between the Federal corporate statutory rate and the company's effective income tax rate:

	1990	1989	1988
Federal corporate statutory rate	(34.0)%	34.0%	38.0%
State and local income taxes, net of Federal tax benefit	7.4	40.0	4.5
Foreign taxes, including foreign currency translation effects	2.4	19.2	0.4
Nondeductible restructuring expenses	—	30.3	—
Tax over book gain on asset dispositions	10.6	—	—
Other	0.5	3.8	—
Effective income tax rate	(13.1)%	127.3%	42.9%

Certain items are recognized for income tax purposes in years other than those in which they are reported in the consolidated financial statements. The sources of these differences are as follows:

	1990	1989	1988
Depreciation	$ 607	$ 1,654	$1,680
Deferred compensation and pension expense	2,542	2,198	62
Valuation and expense accruals	(8,685)	(4,253)	(549)
Inventory costs capitalized	590	(6,462)	(640)
Interest expense	(10,775)	—	—
Other	(64)	25	(227)
	$(15,785)	$(6,838)	$ 326

Future income tax benefits and deferred credits at the end of each fiscal year are included in the accompanying consolidated balance sheet, as follows:

	1990	1989	1988
Prepaid expenses and other current assets	$ 27,243	$ 23,584	$ 7,020
Other long-term liabilities	(15,158)	(33,386)	(29,777)
	$ 12,085	$ (9,802)	$(22,757)

The Federal income tax returns of the company and its major subsidiaries have been examined through fiscal year ended February 28, 1986.

12. EMPLOYEE BENEFITS

The company and its subsidiaries sponsor or contribute to retirement plans covering substantially all employees. The total cost of all plans for fiscal years 1990, 1989 and 1988 was $5,214, $8,695 and $10,058, respectively.

Company Sponsored Defined Benefit Plans — The company follows FASB Statement No. 87 "Employers' Accounting for Pensions." Annual cost for domestic defined benefit plans under Statement No. 87 is determined using the Projected Unit Credit actuarial method. Prior service cost is amortized on a straight-line basis over the average remaining service period of employees expected to receive benefits.

It is the company's practice to fund pension costs to the extent that such costs are tax deductible. Funding decisions made in fiscal 1990 contributed towards the deferred or prepaid pension cost in U.S. plans. The assets of the various plans include corporate equities, government securities, corporate debt securities and insurance contracts.

The tables below provide information on the status of the U.S., company-sponsored, defined benefit plans.

The funded status of the plans is summarized as follows:

	1990		1989		1988	
	Plans in which		Plans in which		Plans in which	
	Assets Exceed Accumulated Benefits	**Accumulated Benefits Exceed Assets**	Assets Exceed Accumulated Benefits	Accumulated Benefits Exceed Assets	Assets Exceed Accumulated Benefits	Accumulated Benefits Exceed Assets
Actuarial present value of benefit obligations:						
Vested benefit obligation	**$202,158**	**$12,523**	$177,422	$ 2,364	$155,423	$11,339
Accumulated benefit obligation	**$206,727**	**$13,910**	$184,918	$ 3,171	$163,194	$11,974
Projected benefit obligation	**$231,852**	**$16,099**	$211,262	$ 3,508	$191,031	$13,657
Plan assets at fair value	**282,715**	**11,536**	257,865	1,207	236,988	9,939
Projected benefit obligation less than (in excess of) plan assets	**50,863**	**(4,563)**	46,603	(2,301)	45,957	(3,718)
Unrecognized net (gain) loss	**(17,124)**	**(2,023)**	(19,047)	25	(18,305)	(1,967)
Unrecognized prior service cost	**822**	—	203	—	—	—
Unrecognized net (asset) obligation at year end	**(23,787)**	**3,009**	(23,233)	978	(26,820)	3,198
Prepaid (accrued) pension cost	**$ 10,774**	**$ (3,577)**	$ 4,526	$(1,298)	$ 832	$ (2,487)

Net periodic pension cost of continuing operations for fiscal years 1990, 1989 and 1988, include the following components:

	1990	1989	1988
Service cost – benefits earned during the period	**$ 4,733**	$ 4,624	$ 5,382
Interest cost on the projected benefit obligation	**19,477**	14,184	13,192
Actual return on plan assets	**(30,282)**	(15,543)	6,385
Net amortization and deferral	**6,631**	437	(20,663)
Net periodic pension cost	**$ 559**	$ 3,702	$ 4,296

The company recognized a curtailment gain of $1,003 associated with continuing operations in fiscal 1990. The company also recognized curtailment gains of $2,774 and $2,388 in fiscal 1990 and 1989, respectively, associated with discontinued operations.

Employees are covered primarily by noncontributory plans, funded by company contributions to trust funds, which are held for the sole benefit of employees. Monthly retirement benefits generally are based upon service, pay, or both, with employees generally becoming vested upon completion of 5 years of service.

The expected long-term rate of return on plan assets was 8.0%-8.5% in fiscal 1990. Measurement of the fiscal 1990 projected benefit obligation was based on an 8.75% discount rate and a 5.5% long-term rate of compensation increase. A discount rate of 9.25% was used in the development of net periodic pension cost for fiscal 1990.

Other Retirement Plans and Benefits – In addition to defined benefit plans, the company makes contributions to various defined contribution, union negotiated and foreign plans. The cost of these plans is included in the total cost for all plans reflected above.

The company has a Savings Plan for Employees of INTERCO INCORPORATED and Affiliates and an INTERCO INCORPORATED Employee Stock Ownership Plan (ESOP). The total cost of these plans for fiscal years 1990, 1989 and 1988 was $447, $548 and $474, net of taxes of $295, $411 and $359, respectively.

The company provides certain health care and life insurance benefits for certain employees who reach retirement age. Retiree health and life insurance benefits are provided through insurance companies. The cost of these benefits is recognized as expense as these claims are paid. Post-retirement health care and life insurance expense for fiscal years 1990, 1989 and 1988 was $397, $1,306 and $1,195, respectively.

13. LEASE COMMITMENTS

Substantially all of the company's retail outlets and certain other real properties and equipment are operated under lease agreements expiring at various dates through the year 2022. Leases covering retail outlets and equipment generally require, in addition to stated minimums, contingent rentals based on retail sales and equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates.

Rental expense under operating leases for fiscal years 1990, 1989 and 1988, was as follows:

	1990	1989	1988
Basic rentals	**$33,701**	$33,323	$27,506
Contingent rentals	**23,845**	31,849	28,230
	57,546	65,172	55,736
Less sublease rentals	**3,241**	1,729	568
	$54,305	$63,443	$55,168

Included in rental expense above is the cost of services provided by lessors of leased retail departments, estimated to aggregate $7,800, $15,100 and $17,800 in fiscal years 1990, 1989 and 1988, respectively.

Future minimum lease payments under operating leases, reduced by minimum rentals from subleases of $12,540, at February 24, 1990, aggregate $131,413. Annual payments under operating leases are $28,893, $23,805, $18,751, $15,046 and $11,539 for fiscal years 1991 through 1995, respectively.

The company has also guaranteed leases of the discontinued operations which at February 24, 1990 aggregated approximately $50,652, based on minimum rentals.

14. LITIGATION

In fiscal 1989, certain shareholder actions were filed against the company and its directors in the United States District Court for the Southern District of New York and the Delaware Court of Chancery. These actions allege, among other things, that the directors of the company violated the federal securities laws and breached their fiduciary duties to the company's shareholders in connection with Cardinal Acquisition Corp.'s tender offer for the company's stock. The suits seek damages and other remedies. These shareholder actions have now been settled, pending approval of that settlement by the courts.

In fiscal 1990, the company filed suit against Spirit Holding Company, Inc., the purchaser of the company's Central Hardware Company subsidiary, alleging that Spirit had failed to pay the company a portion of the purchase price. Spirit filed a counterclaim, alleging breaches of certain representations and warranties on the part of the company, and seeking damages. The company filed an amended complaint to include certain present and former members of Central Hardware Company management in the action, alleging that if any such breaches of representations and warranties occurred, they were the result of faulty information provided by Central Hardware Company management, in breach of certain incentive compensation agreements. The company believes the Spirit counterclaim is without merit and intends to defend against it vigorously.

Subsequent to fiscal 1990, the trustee under the company's medium term note indenture dated November 1, 1987, filed suit against the company and the two trustees under the Secured Credit Agreement. This action seeks a declaration of the respective rights of the medium term note holders and the company's lending banks, and seeks to determine whether effective provision has been made to secure the medium term notes equally and ratably as required by the medium term note indenture. The suit also seeks other equitable and injunctive relief, primarily with respect to the sharing of the proceeds of the company's asset sales. The company believes this suit is without merit and intends to defend against it vigorously.

In the opinion of management, after consultation with the company's legal counsel, these claims when resolved, either individually or in the aggregate, will not have a material adverse effect on the consolidated financial condition of the company and its subsidiaries.

The company is or may become a defendant in a number of pending or threatened legal proceedings in the ordinary course of business. In the opinion of management, the ultimate liability, if any, of the company from all such proceedings will not have a material adverse effect upon the consolidated financial condition of the company and its subsidiaries.

15. BUSINESS SEGMENT INFORMATION

The company's two business segments are the Footwear Manufacturing and Retailing Group and the Furniture and Home Furnishings Group. Information, on an unaudited basis, relating to the operating companies and their products, which comprise each segment, is included on the inside front cover. Summarized financial information by business segment is as follows:

	1990	1989	1988
Net sales to unaffiliated customers:			
Footwear	**$ 745,676**	$ 915,447	$ 890,411
Furniture	**910,403**	1,096,515	1,105,563
Total	**$1,656,079**	$2,011,962	$1,995,974
Operating earnings:			
Footwear	**$ 48,662**	$ 45,565	$ 92,204
Furniture	**101,488**	131,731	149,090
	150,150	177,296	241,294
Corporate and restructuring expenses, interest expense, and other income	**(208,716)**	(161,601)	(42,557)
Earnings (loss) from continuing operations before income taxes	**$ (58,566)**	$ 15,695	$ 198,737
Identifiable assets at year end:			
Footwear	**$ 526,633**	$ 595,977	$ 595,861
Furniture	**426,593**	715,636	688,853
	953,226	1,311,613	1,284,714
Discontinued operations	**114,847**	346,372	521,644
Corporate assets	**80,237**	117,317	24,042
Total	**$1,148,310**	$1,775,302	$1,830,400
Depreciation expense:			
Footwear	**$ 13,346**	$ 13,694	$ 13,107
Furniture	**20,105**	24,964	26,208
Capital expenditures:			
Footwear	**$ 7,611**	$ 14,020	$ 9,236
Furniture	**22,049**	38,635	36,188

As discussed in Note 4, the company disposed of its Ethan Allen Inc. subsidiary on June 29, 1989 and a substantial part of Senack Shoes, Inc. on September 18, 1989. Ethan Allen's operating results are included in the furniture segment and Senack's in the footwear segment through the dates of disposal.

Operating earnings of each business segment include its sales less all operating expenses. Substantially all of the company's sales are made to unaffiliated customers. No customer accounted for 10% or more of consolidated sales. Foreign operations are not material.

Identifiable assets are those assets used by each segment in its operations. Corporate assets consist primarily of cash, short-term investments and unamortized deferred debt costs.

16. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Following is a summary of unaudited quarterly information for each of the years in the three-year period ended February 24, 1990.

	First	Second	Third	Fourth
Net Sales:				
1990	$468,654	$430,198	$376,923	$380,304
1989	490,062	491,335	547,449	483,116
1988	472,944	474,248	548,605	500,177
Gross Profit:				
1990	$162,175	$145,382	$118,507	$132,457
1989	173,989	164,052	181,551	156,692
1988	168,626	167,497	188,173	182,930
Net Earnings (Loss) From Continuing Operations:				
1990	$ (41,451)	$ 41,451	$ (32,997)	$ (17,878)
1989	23,756	18,689	(4,576)	(42,151)
1988	19,332	24,896	36,762	32,444
Net Earnings (Loss) From Discontinued Operations:				
1990	$ 9,851	$ 77,210	$ 4,475	$ (5,454)
1989	6,933	16,192	15,082	36,225
1988	7,182	13,533	6,687	4,167
Net Earnings (Loss):				
1990	$ (31,600)	$118,661	$ (28,522)	$ (23,332)
1989	30,689	34,881	10,506	(5,926)
1988	26,514	38,429	43,449	36,611
Earnings (Loss) Per Share From Continuing Operations:				
1990	$ (1.54)	$ 0.52	$ (1.37)	$ (0.98)
1989	0.62	0.50	(0.11)	(1.43)
1988	0.45	0.58	0.89	0.82
Net Earnings (Loss) Per Share:				
1990	$ (1.29)	$ 2.43	$ (1.25)	$ (1.11)
1989	0.80	0.93	0.29	(0.49)
1988	0.62	0.90	1.05	0.93
Common Dividends Paid Per Share:				
1990	$ 0	$ 0	$ 0	$ 0
1989	0.430	0.455	38.600	27.450
1988	0.400	0.400	0.400	0.400
Common Stock Price Range (Closing High-Low):				
1990	$ 3⅝-2	$ 3-1⅝	$ 1¾-9/16	$ ¾-9/32
1989	46-40	73-41	73-29	32-2⅝
1988	46-38	54-40	53-30	42-30

The closing market price of INTERCO's Common and Series E Preferred Stock at fiscal year end 1990 was $0.41 and $1.00 per share, respectively.

During the fourth quarter of fiscal 1990, gross profit margins were 34.8% as compared to 32.4% in fiscal 1989 and 36.6% in fiscal 1988. Margins in fiscal 1989 were adversely impacted by the results of the Footwear Manufacturing and Retailing Group due to promotional costs and unfavorable manufacturing variances resulting from the sales decline in canvas footwear, and manufacturing start-up costs within the athletic footwear segment.

Independent Auditors' Report

The Board of Directors and Shareholders
INTERCO INCORPORATED

We have audited the accompanying consolidated balance sheets of INTERCO INCORPORATED and subsidiaries as of February 24, 1990, February 25, 1989 and February 29, 1988, and the related consolidated statements of earnings and changes in shareholders' equity (deficit) for each of the years in the three-year period ended February 24, 1990, the consolidated statements of cash flows for the years ended February 24, 1990 and February 25, 1989, and the consolidated statement of changes in financial position for the year ended February 29, 1988. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of INTERCO INCORPORATED and subsidiaries at February 24, 1990, February 25, 1989 and February 29, 1988, the results of their operations for each of the years in the three-year period ended February 24, 1990, their cash flows for the years ended February 24, 1990 and February 25, 1989, and their changes in financial position for the year ended February 29, 1988 in conformity with generally accepted accounting principles.

The accompanying consolidated financial statements have been prepared assuming that the company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the company has a substantial portion of its debt due contractually within the next fiscal year and expects not to be in compliance with certain financial covenants contained in certain of its credit agreements, which will permit its lenders to accelerate the due dates on its debt. The company's inability to meet its liquidity needs raises substantial doubt about the company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty. As described in Note 2, to alleviate its liquidity problems, the company is seeking to implement a restructuring plan to achieve changes in its debt and capital structure, including an amended bank agreement and the exchange of existing debentures and preferred stock for new debentures and common stock.

As discussed in Note 1 to the consolidated financial statements, the company adopted Statement of Financial Accounting Standards No. 95 "Statement of Cash Flows" in fiscal 1989.

KPMG Peat Marwick

St. Louis, Missouri
April 9, 1990, except for certain
information in Notes 2, 7 and 8,
as to which the date is May 4, 1990

Five Year Consolidated Financial Review

(Dollars in thousands except per share data)

Years Ended	1990	1989	1988	1987	1986
For The Year					
Summary of operations:					
Net sales	**$ 1,656,079**	$ 2,011,962	$1,995,974	$1,630,918	$1,462,766
Cost of sales	**1,097,558**	1,335,678	1,288,748	1,051,110	943,970
Interest expense	**303,123**	141,735	29,188	23,061	20,888
Earnings (loss) from continuing operations before income taxes	**(58,566)**	15,695	198,737	154,805	136,549
As a percent of net sales	**(3.5)%**	0.8%	10.0%	9.5%	9.3%
Income taxes	**(7,691)**	19,977	85,303	71,321	65,040
Net earnings (loss) from continuing operations	**(50,875)**	(4,282)	113,434	83,484	71,509
As a percent of net sales	**(3.1)%**	(0.2)%	5.7%	5.1%	4.9%
Discontinued operations	**86,082**	74,432	31,569	42,290	48,340
Net earnings (loss) applicable to common stock	**(48,631)**	58,366	145,003	125,774	119,853
Per share of common stock:					
Earnings (loss) from continuing operations	**$(3.37)**	$(0.42)	$2.74	$1.93	$1.64
Net earnings (loss)	**$(1.22)**	$1.53	$3.50	$2.91	$2.75
Cash dividends	**$ –**	$39.49	$1.60	$1.57	$1.54
Securities dividends	**$ –**	$27.45	$ –	$ –	$ –
Average common and common equivalent shares outstanding (in thousands)	**39,998**	38,262	41,456	43,312	43,608
Cash dividends paid:					
On common stock	**$ –**	$ 1,454,218	$ 59,598	$ 53,273	$ 51,080
On preferred stock	**$ –**	$ 1,944	$ 4,621	$ 4,972	$ 5,405
At Year End					
Working capital	**$(1,255,696)[1]**	$ 451,609	$ 985,956	$ 928,427	$ 966,228
Property, plant and equipment, net	**186,919**	327,070	317,238	312,782	270,811
Capital expenditures	**29,663**	53,829	45,925	34,435	36,211
Total assets	**1,148,310**	1,775,302	1,830,400	1,741,809	1,587,965
Long-term debt	**3,176 [1]**	1,178,180	266,191	143,358	134,799
Debentures	**– [1]**	808,657	–	–	–
Shareholders' equity (deficit)	**(966,568)**	(1,005,750)	1,251,337	1,326,215	1,280,153

[1] As discussed in Notes 7 and 8 to the Consolidated Financial Statements, $600,536 of long-term debt and $885,265 of debentures were reclassified as current liabilities as of February 24, 1990.

Board of Directors and Corporate Officers

BOARD OF DIRECTORS

Ronald L. Aylward 1,5
Vice-Chairman of the Board of the Company

William E. Cornelius 2*,4
Chairman of the Board and Chief Executive Officer of Union Electric Company

Donald E. Lasater 1,2,3*,4,5
Retired Chairman of the Board and Chief Executive Officer of Mercantile Bancorporation Inc.

Lee M. Liberman 2,3,4*
Chairman of the Board, President and Chief Executive Officer of Laclede Gas Company

Richard B. Loynd 1,5
President and Chief Executive Officer of the Company

R. Stuart Moore
Chairman of the Board of The Lane Company, Incorporated

Thomas H. O'Leary 2,3,4,5
President and Chief Executive Officer of Burlington Resources Inc.

Robert H. Quenon 4,5*
President and Chief Executive Officer of Peabody Holding Co., Inc.

Harvey Saligman 1*
Chairman of the Board of the Company

CORPORATE OFFICERS

Harvey Saligman
Chairman of the Board

Richard B. Loynd
President and Chief Executive Officer

Ronald L. Aylward
Vice-Chairman of the Board

Eugene F. Smith
Executive Vice-President

Charles J. Rothschild, Jr.
Vice-President

R. Stuart Moore
Vice-President

Ronald J. Mueller
Vice-President

Duane A. Patterson
Secretary

Robert T. Hensley, Jr.
Treasurer

Stanley F. Huck
Assistant Vice-President, Finance

David P. Howard
Controller

Keith E. Mattern
General Counsel and Assistant Secretary

James K. Pendleton
Assistant Secretary

William R. Withrow
Assistant Treasurer

Committees of the Board

1 Executive Committee

2 Audit Committee

3 Executive Compensation and Stock Option Committee

4 Finance Committee

5 Nominating Committee

(*indicates Committee Chairman)

Principal Companies of INTERCO

CORE OPERATING COMPANIES

Furniture and Home Furnishings Group

Broyhill Furniture Industries, Inc.
Lenoir, North Carolina

The Lane Company, Incorporated
Altavista, Virginia

Footwear Manufacturing and Retailing Group

The Florsheim Shoe Company
Chicago, Illinois

Converse Inc.
North Reading, Massachusetts

OTHER OPERATING COMPANIES

Abe Schrader Corporation
New York, New York

Megastar Apparel Group
Paramus, New Jersey

Senack Shoes, Inc.
St. Louis, Missouri

Sky City Stores, Inc.
Asheville, North Carolina

Transfer Agents, Registrars and Dividend Disbursing Agent Common and Preferred Stock

Transfer Agents and Registrars
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

First Chicago Trust Company of New York
30 West Broadway
New York, New York 10001-2192
(212) 587-6434

Dividend Disbursing Agent
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Exchange Listings
Common Shares are listed on the New York Stock Exchange and the Midwest Stock Exchange. (Trading symbol: ISS)

Trustees, Registrars and Paying Agents Notes and Debentures

Trustee, Registrar and Paying Agent for
8.875% Promissory Notes due 1993
The Boatmen's National Bank of St. Louis
Corporate Trust Department
510 Locust Street
St. Louis, Missouri 63101
(314) 436-9581

Trustee, Registrar and Paying Agent for
8.45% Promissory Notes due 1993
8.30% Promissory Notes due 1992
7.95% Promissory Notes due 1991

Trustee:
The Boatmen's National Bank of St. Louis
Corporate Trust Department
510 Locust Street
St. Louis, Missouri 63101
(314) 436-9581

Registrar and Paying Agent:
Bankers Trust Company
Corporate Trust and Agency Group
4 Albany Street
New York, New York 10006
(212) 250-6000 (Shareholder Relations)

Trustee, Registrar and Paying Agent for 13.75% Senior Subordinated Debentures due 2000
First Trust National Association
108 East Fifth Street
St. Paul, Minnesota 55101
(612) 223-7069

Trustee, Registrar and Paying Agent for 14.00% Subordinated Discount Debentures due 2003
Norwest Bank Minnesota N.A.
Sixth Street & Marquette Avenue
Minneapolis, Minnesota 55479
(612) 667-9528

Trustee, Registrar and Paying Agent for 14.50% Junior Pay-in-Kind Subordinated Debentures due 2003
Trustee:
Connecticut National Bank
777 Main Street
Hartford, Connecticut 06115
(203) 722-9082

Registrar and Paying Agent:
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Corporate Offices
101 South Hanley Road
St. Louis, Missouri 63105
(314) 863-1100

Annual Meeting
The Annual Meeting of Shareholders will be held at 10 a.m., Monday, June 25, 1990, at the Clayton Community Center, Two Mark Twain Circle, Clayton, Missouri. Notice of the meeting and a proxy statement will be sent to shareholders in a separate mailing.

Trademarks and Trade Names
The trademarks, trade names and licensed trademarks of INTERCO and its subsidiaries appearing in the Annual Report, are italicized.

Form 10-K Annual Report
A copy of the current Form 10-K filed with the Securities and Exchange Commission can be obtained by writing to the Treasurer of INTERCO at the Corporate Offices.

Independent Auditors
KPMG Peat Marwick
1010 Market Street
St. Louis, Missouri 63101
(314) 444-1400

INTERCO INCORPORATED
St. Louis, Missouri